



U.S. SMALL BUSINESS ADMINISTRATION **EX PARTE OR LATE FILED**
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FEDERAL COMMUNICATIONS COMMISSION
OFFICE OF THE SECRETARY

The Honorable William E. Kennard
Chairman
Federal Communications Commission
1919 M Street NW Suite 814
Washington, DC 20554

RE: Ex Parte Presentation in a Non-Restricted Proceeding
In re Amendment of Part 1 of the Commission's Rules -- Competitive Bidding Procedures,
WT Docket No. 97-82

Dear Chairman Kennard:

The Office of Advocacy, U.S. Small Business Administration ("Advocacy") shares the Federal Communications Commission's ("FCC" or "Commission") concern that only truly deserving small businesses should receive the benefits of its small business competitive bidding incentives (i.e. bidding credits, favorable down payment and interest terms, and installment payments). To this end, we respectfully request that the Commission reconsider whether an asset test should also be required as a factor in defining a "small business concern" for competitive bidding purposes.¹ We believe that a complete review of this issue would complement the Commission's current evaluation of whether to adopt a "controlling interest standard" or imposition of a "minimum equity requirement" in its reconsideration of its Part I Competitive Bidding rulemaking.² We also inquire whether the Commission will consider application of these comments in the proceeding to reauction C Block licenses.³

It is extremely relevant that the Commission's small business incentives were designed to fulfill the statutory objectives of the Communications Act of 1934, as amended, by "promoting economic opportunity and competition and ensuring that new and innovative technologies are readily accessible to the American people by avoiding excessive concentration of licenses and by disseminating licenses among a wide variety of applicants, including small businesses, rural

¹ Per the request of the Wireless Telecommunications Bureau, this ex parte comment documents for the record Advocacy's request for further review of the FCC's definition of small business concerns. Previous discussions between the FCC and SBA were in the scope of permissible interagency communications given the U.S. Small Business Administration's ("SBA") statutory authority to approve all alternative small business size standards. 15 U.S.C. § 632(a)(2)(C).

² In re Amendment of Part I of the Commission's Rules -- Competitive Bidding Procedures, WT Docket No. 97-82, Third Report and Order and Second Further Notice of Proposed Rulemaking, 13 FCC Rcd 10274 (1997) ("Third R & O").

³ In re Amendment of the Commission's Rules Regarding Installment Payment Financing for personal Communications Services (PCS) Licensees, Fourth Report and Order, WT Dkt. No. 97-82, FCC 98-176 (rel. Aug. 19, 1998).

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telephone companies, and businesses owned by members of minority groups and women” 47 U.S.C. § 309(j)(3)(B). Congress recognized that small businesses, minorities, and women-owned businesses do not have ready access to capital nor the resources to acquire telecommunications licenses for reasons unrelated to competence.⁴ Therefore, Congress directed the Commission to consider special incentives to promote economic opportunities for these designated entities that compensated for the lack of ready access to capital.⁵

Advocacy appreciates the Commission’s efforts to provide innovative and flexible rules as a means to secure financing and to level the playing field in this regard for traditional small businesses. However, Advocacy is concerned that reported developments in recent auctions may have actually served to preclude traditional small businesses from participation in the Commission’s competitive bidding process, contrary to congressional intent.⁶ Although these reports of “unqualified” small businesses that should not have been eligible for benefits have been contested,⁷ we believe there remains a great potential for manipulation and abuse of the Commission’s definitions for small business given the increasing demand for electromagnetic spectrum and the value of the benefits that small businesses receive in the auction process.

Advocacy acknowledges the measures that the Commission has already taken to prevent such abuse, including refinement of its affiliation rules to include an “indicia of control” standard that “help[s] to ensure that businesses seeking small business status are truly small.” Third R & Q, para. 27. We also recognize that the difficulty of this rulemaking lies in granting legitimate small businesses the flexibility to raise capital and secure investors from a variety of sources for capital intensive telecommunications services while ensuring that the Commission’s small business classification does not become illusory nor its criteria eviscerated.

Some traditional small businesses have been very successful in raising capital and forming relationships with large companies and/or well financed individuals. This is commendable. It is not Advocacy’s intent, nor do we believe that it is the Commission’s, to stifle nor undermine those efforts. We are simply concerned that every protective measure should be considered as a means to address innovative schemes and unique business structures that are inconsistent with the statutory objectives of leveling the playing field for legitimate small businesses.

⁴ See H.R. Rep. No. 103-111, at 254-55 (1993) (“[U]nless the Commission is sensitive to the need to maintain opportunities for small businesses, competitive bidding could result in a significant increase in concentration in the telecommunications industries. . . . One of the primary criticisms of utilizing competitive bidding to issue licenses is that the process could inadvertently have the effect of favoring only those with ‘deep pockets’, and therefore have the wherewithal to participate in the bidding process.”).

⁵ Id. at 255.

⁶ Mike Mills, In Next FCC Auction, the Wealthy Will Get the Discount, Wash. Post, Feb. 12, 1998, at D1.

⁷ See, e.g., Thomas H. Jones, Letter to the Editor, Individual Entrepreneurs, Wash. Post, Mar. 3, 1998, at A16; see also William E. Kennard, Letter to the Editor, Auctioning the Broadcast Spectrum, Wash. Post, Feb. 26, 1998, at A14.

For example, a new small business created as a spin-off, but not an affiliate nor subsidiary, of a larger entity does not have the same difficulty accessing capital nor do they have the limited resources and lack of support that a traditional small business may have. Such newly formed "small business" entities may be technically legal under the Commission's current rules given the absence of gross revenue. However, while Congress anticipated new entrant participation in the auction process, Advocacy believes that any receipt of FCC small business auction incentives by such "spin-off" entities clearly contravenes the expressed intent of Congress in 47 U.S.C. § 309(j) to provide assistance to small businesses that need access to capital. Ideally, the Commission's affiliation and attribution rules would operate as safeguards to prevent such a circumstance. We are, however, not confident that these rules are sufficient for all foreseeable scenarios. Nor does the "flexibility" of the FCC's rules provide enough guidance for an entity to ascertain properly whether it warrants small business eligibility prior to the commencement of the auction.⁸

The FCC has noted that the SBA does not use an asset test in its classification of a small business concern.⁹ However, the SBA's regulations do include a "spin-off rule" in which "[a] firm will not be treated as a separate business concern if a substantial portion of its assets and/or liabilities are the same as those of a predecessor entity." 13 C.F.R. § 121.105(c) (emphasis added). Under the SBA's regulations, the predecessor entity's annual receipts/revenue will be attributable to the newly formed entity. Id. The FCC's rules do not explicitly include such a test nor is one proposed. Therefore, public comment on the following questions may be helpful. Would the adoption or modification of the SBA's "spin-off rule" for determination of assets be helpful or are the FCC's affiliation rules sufficient to address this scenario? If addition of a "spin-off rule" would be helpful, how should "substantial portion" be defined? In general, how should assets be defined (e.g., lines of credit, equipment and/or construction contracts, real estate holdings, telecommunications licenses and/or franchises)? How should assets be valued/measured? How would such a rule be applied in conjunction with the Commission's affiliation and attribution rules?

The value of an asset test for the FCC's competitive bidding proceeding is distinguishable from the SBA's. First, if the SBA were to use an asset test, the primary need would be for the SBA's government procurement and guaranteed loan programs. For this purpose, assets are often

⁸ In some instances, Advocacy believes that the "Petition to Deny" process may not be adequate to address designated entity eligibility given that the auction has already been completed and the burden is on the FCC to expedite the licensing process and facilitate service to the public as quickly as possible. The harm inherent in this circumstance is even more egregious for auctions that are exclusively for small businesses, such as PCS C and F blocks, because an unqualified small business entity will have distorted the outcome of the auction for eligible small businesses.

⁹ See e.g., Third R & O, para. 19 ("[W]hile we have used a total assets test in determining eligibility for entrepreneur blocks, we have not used such a test for determining small business eligibility.") (citations omitted); see also In re Amendment of the Commission's Rules Concerning Maritime Communications, Third Report and Order and Memorandum Opinion and Order, PR Dkt. No. 92-257, RM-7956, 8031, 8352, FCC 98-151, para. 66 (rel. July 9, 1998).

difficult to value and ascertain, particularly over the long run of a business' operation. However, the FCC need only take a snapshot of a new entrant/small businesses' profile in the early stages of the competitive bidding process. Second, the SBA's more restrictive affiliation rules (and thus, attribution rules) in addition to the "spin-off rule" mentioned previously are, in the aggregate, sufficient to compensate for not using an asset test.¹⁰

Finally, application of an asset test would be administratively burdensome for the SBA for use in procurement and loan applications given the large volume of decisions that need to be made quickly,¹¹ and the difficulty in getting verifiable data in short amounts of time.¹² Conversely, the FCC's evaluation of a business' assets is only done once in the initial stages of licensing for individual auctions and there are usually no statutory nor regulatory restrictions on the time frame for the FCC's evaluation of an applicant's qualifications. Therefore, asset information can be verifiable for the FCC given the longer time the FCC has to evaluate the long-form applications [FCC Form 600] of a winning bidder.

Advocacy also believes that it would be prudent and more efficient for an entity to have better guidance of whether it is eligible for designated entity status before the auction commenced and not to rely solely on the Commission's "Petition to Deny" process. To this end, we propose that the Commission identify "red flag" areas that could indicate problem issues for a potential bidder in its eligibility to bid as a designated entity. For example, the origin of a new firm's capitalization, or a commonality of not only directors and officers between two companies but employees and/or principal investors as well, could indicate "control" and therefore, affiliation. This guidance does not preclude the FCC from its flexibility in using a subjective test in its evaluation of a licensee's qualifications.

¹⁰ Although the FCC's affiliation rules are similar to the SBA's in regards to the "indicia of control" factor, the FCC has several exceptions to application of its affiliations rule. For example, in PCS C Block, all small businesses can exclude from affiliation rules any of its affiliates if the affiliate qualifies as an entrepreneur [\$125 million gross revenue and \$500 million total assets] and the total assets and gross revenue of all such affiliates on a cumulative basis do not exceed the aforementioned entrepreneur limits. In re Implementation of Section 309(j) of the Communications Act - Competitive Bidding, Sixth Report and Order, 10 FCC Rcd 136, para. 33 (1995). While these exceptions serve to promote a small business' ability to secure large investors (often necessary given the nature of the service), they also have the potential to help circumvent the FCC's eligibility requirements for designated entities. Therefore, additional safeguards may be necessary.

¹¹ For example in 1997, there were 27,602 contract actions in SBA's 8(a) Minority Enterprise Development program. A Report to the U.S. Congress on Minority Small Business and Capital Ownership Development for Fiscal Year 1997, U.S. Small Business Administration, Office of Enterprise Development, at 3.


¹² See, e.g. 13 C.F.R. §§ 121.1004 - 121.1005, 121.1009 (requiring specific time frames for the SBA's review, approval and resolution of any protests to "formal size determinations," especially pertaining to the award of a federal contract).

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In summary, the Office of Advocacy respectfully recommends that the Commission include questions in its Further Notice of Proposed Rulemaking whether an asset test should be a factor in determining small business eligibility for competitive bidding purposes, whether its current affiliation and attribution rules are sufficient to ensure that true small businesses are the beneficiaries of the FCC's bidding incentives or need to be fine-tuned, and whether there should be identification of "red flag" indicia of control factors.

Thank you for your consideration of these comments. Advocacy looks forward to working with the Commission in its review of these issues.

Sincerely,


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